

CANADA-U.S. FREE TRADE AGREEMENT



SUMMARY
ELABORATIONS AND CLARIFICATIONS
TO THE
ELEMENTS OF THE AGREEMENT
AS REFLECTED IN THE LEGAL TEXT
OF THE
FREE TRADE AGREEMENT
BETWEEN CANADA
AND THE
UNITED STATES OF AMERICA



TRADE:
Securing
Canada's
Future

Canada

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INTRODUCTION:

Over the past two months, officials from Canada and the United States have translated the October 4th framework agreement into legal language. Officials have clarified the precise legal meaning of The Elements of the Agreement and elaborated on the details, ensuring that the balance of benefits is maintained.

PART ONE: OBJECTIVES AND SCOPE

Chapter 1: Objectives and Scope

Article 105: National Treatment

This article provides that to the extent provided in the trade agreement, each Party shall provide national treatment with respect to investment and to trade in goods and services.

The concept of national treatment is a basic liberalizing principle of international trade law. It is the foundation on which many of the obligations of the GATT and the Canada-U.S. Trade Agreement are built. The particular applications of national treatment and exceptions to it are specified in individual chapters.

Chapter 2: General Definitions

PART TWO: TRADE IN GOODS

Chapter 3: Rules of Origin for Goods

Annex 301.2: Interpretations

The general rule of origin for goods to receive duty free treatment for shipments between the Parties is a change of tariff classification. For a number of industries (e.g. chemicals, footwear, machinery, electronic, autos) this rule is supplemented by a 50% cost of production test to ensure that the benefits of the FTA tariff treatment will accrue to Canadian or US producers. The methodology agreed to for this test provides that duty and taxes on materials originating outside Canada or the United States and inland freight, although incurred in Canada or the United States, will be treated as foreign content whereas the total value of offshore components that meet the rules of origin will count towards the 50%.

Apparel made from offshore fabrics will qualify for preferential FTA treatment into the U.S., up to the following levels: 50 million square yards for non-woollen apparel and 6 million square yards for woollen apparel. Above these levels, apparel made from offshore fabrics will face MFN rates into the U.S., but can benefit from duty drawbacks. Apparel made from Canadian or U.S. fabrics will qualify for preferential FTA treatment into the U.S. The corresponding levels for apparel exported to Canada from the United States are 10.5 million square yards for non-woollen apparel and 1.1 million square yards for woollen apparel.

Fabrics made in Canada from offshore yarns and exported to the United States will qualify for preferential entry under the FTA, up to an annual level of 30 million square yards. This quota arrangement will continue until December 31, 1992 and will be reviewed within two years of implementation of the Agreement in order to work out a solution satisfactory to both Parties countries. There will be no corresponding level for fabric exports from the United States to Canada.

The FTA rules of origin have been specifically designed to prevent goods processed offshore and returned to the USA at reduced rates under the US tariff 807 provision from qualifying for preferential FTA treatment. This provision is used by US companies operating in Mexico.

Chapter 4: Border Measures

Article 401: Tariff Removal

Tariffs on certain telecommunications products such as telephone sets and switching apparatus will be removed immediately on January 1, 1989 or to three annual steps.

Article 407: Import and Export Restrictions

407.2 specifies the parties' understanding that their existing GATT obligations prohibit minimum import or export price requirements.

407.3 makes it clear that when one country imposes an import control on a product of a specified third country, the other Party will not serve as a conduit to the first Party; it also allows for the adding as a condition to any exoneration from export controls for bilateral trade that the product involved be consumed in the other Party.

407.4 provides for consultations about actions to be taken in circumstances where either Party might create a distortion in bilateral trade by implementing a restriction on imports of a good from third countries.

Article 408: Export Taxes

This article makes it clear that neither Party will impose export taxes (i.e. taxes over and above those levied on domestic sales) on exports to each other.

Article 409: Other Export Measures

409.1 (a) specifies the GATT circumstances (conservation, short supply, domestic price stabilization schemes) in which the use of an export control by either country will be accompanied by proportionate allocation of the reduced supply. It specifies that in these circumstances, the export control cannot reduce the amount available for export below the amount exported relative to the total supply which prevailed in the most recent 36-month period. Total supply is defined as being all shipments from domestic production, domestic inventories and other imports as appropriate.

409.1 (b) requires that the export control not require the disruption of normal channels of distribution or of the normal product mix of the goods subject to the control.

Chapter 5: National Treatment

Article 501, 502: Incorporation of GATT Rule, Provincial and State Measures

Article 501 incorporates the United States' and Canada's existing national treatment obligations under the General Agreement on Tariffs and Trade for Part Two: Trade in Goods. Similarly, Article 502 provides for the states and provinces to give treatment no less favourable than the most favourable treatment provided by the province or state to goods from the other Party.

Chapter 6: Technical Standards

Article 605: Accreditation

Provides for accreditation of each other's certification bodies.

Chapter 7: Agriculture

Article 702: Special Provisions for Fresh Fruits and Vegetables

The conditions under which the existing tariffs on fresh fruits and vegetables can be reapplied are spelled out.

The text states that where the import price is below 90% of the previous five-year average monthly import price and the planted acreage of the importing Party is not higher than the previous five-year average (taking out the high and low year), the MFN tariff rate can be re-applied on a temporary basis. The text ensures that planted acreage increases, as a result of possible shifts from wine grape production to other fruits and vegetables are excluded from acreage calculation. This is a new element which will be of assistance to grape growers who may be facing adjustment over the next few years and wish to shift from grape to such crops as tender tree fruits.

In the absence of this provision recourse to the 20-year tariff "snap-back" provision for some fruits and vegetables could have been prevented because of acreage increases arising from wine grape adjustments.

In addition, the text notes that the tariff can only be applied once a year nationally or once per year per region, and that its duration will be for a maximum of 180 days.

Two days' notice and consultations are required before application of the tariff.

The text then lists the products covered by this article (all fresh fruits and vegetables, except those that are already duty free).

Article 704: Market Access for Meat.

Article 704.1 provides that both countries will exclude each other from the provisions of their respective Meat Import Laws.

Article 704.2 spells out that when a Party takes action against third party imports and the other Party does not take similar action, the Agreement contains a provision aimed at avoiding displacement which could frustrate the effect of the quantitative restrictions on third country imports.

Article 705: Market Access for Grain and Grain Products

The elements text indicates that import permits will be removed when "support levels" are equalized. The legal text spells out the details of the "technical calculation". In addition, the text indicates that if import restrictions are lifted, Canada reserves the right to require end-use certificates or denaturing to ensure that the integrity of the Canadian grain quality control system is maintained.

The use of end-use certificates will ensure that U.S. grain does not enter Canada's grain handling system and thereby ensures that no U.S. grain is mixed with Canadian grain destined for export to third countries.

Article 706: Market Access for Poultry and Eggs

The elements text indicated that Canada would increase its global import quotas for poultry, eggs and products. The legal text spells out the actual size of the new quotas. The increases in the poultry import quotas are to agreed specified levels based on the 1982-86 actual import levels. There will be no subsequent re-calculation.

- . The chicken import quota will increase from 6.3% to 7.5% of domestic production.
- . The turkey import quota will increase from 2% to 3.5% of domestic production.
- . The shell egg import quota will increase from 0.675% to 1.647% of domestic shell egg production.
- . The liquid, frozen and further processed egg import quota will increase from 0.415% to 0.714% of domestic shell egg production.
- . The powdered egg import quota will increase from 0.615% to 0.627% of domestic shell egg production.

Article 707: Market Access for Products Containing 10 Percent or Less Sugar

The elements text referred to "sweeteners". The legal text refers to "sugar". This change ensures that in determining the eligibility of a product for this exemption, sweeteners other than sugar will not be included in the 10 per cent calculation.

Article 708: Technical Regulations and Standards for Agricultural, Food, Beverage and Certain Related Goods

This article sets out in detailed form the principles to govern technical regulations and standards and establishes eight working groups to further the implementation of this section. Canada and the United States have agreed to work towards greater compatibility of technical regulations for these goods. This compatibility will not result in the lowering of any Canadian standards. In addition, the text guarantees that an open border policy for meat inspection will be maintained and limited to occasional spot checks to ensure compliance with inspection requirements. In addition, the text contains twelve schedules in an annex that sets out, for each specific area, guidelines for implementation.

Article 710: International Obligations

This article specifically provides that both Canada and the United States maintain their rights and obligations under Article XI of the GATT. This ensures that Canada may maintain import quotas necessary to protect existing or new national supply management programs.

Chapter 8 Wine and Distilled Spirits

Chapter 8 provides a detailed elaboration of the obligations which were agreed to in the Elements of the Agreement.

Article 803: Pricing

The wording sets out with specific dates, the timetable agreed to in the elements.

Article 804.3: Distribution

This article makes clear that the provision to grandfather Quebec grocery store sales of wine applies to the province of Quebec. In addition, the text clarifies that outlets (i.e. SAQ) must be available to distribute imported U.S. wine.

Article 808: Definitions

The definitions section clarifies that for Article 804, wine store outlets that are grandfathered are those in operation, in the process of being built, or where an application had been approved.

This will ensure that those companies who had received provincial approval and had made commercial plans and commitments will be able to carry through with their approved stores.

Chapter 9: Energy

The Energy Chapter has given rise to a number of misunderstandings as to its scope and content since the publication of the Elements of Agreement. The text in a very detailed and clear way translates faithfully the Elements in a way which Canadians will see safeguards our energy interests.

It makes very clear that Canada has no obligation to supply energy to the U.S. However, in cases of short supply, cutbacks in exports to the U.S. and the administration of the cutbacks would be done in a fair way. The proportionality test for energy is identical to that provided for all other goods.

The text acknowledges and indeed allows for higher prices for export sales arising from the application of a quantitative restriction but specifies that it should not be imposed by government action.

In the Elements of the Agreement, Canada undertook to eliminate only one of the three price tests the National Energy Board applies to exports. The least cost alternative test is being eliminated. In addition the text makes clear that surplus tests can continue to be operated by either party.

Article 902: Import and Export Restrictions

902.1 and 902.2 make clear that the trade agreement's rights and obligations with respect to energy trade restrictions are the GATT reasons for which such measures can be taken. The obligations apply to imports and exports, and apply equally to both Parties.

902.4 provides for consultations about actions to be taken in circumstances where either Party might create a distortion in bilateral trade by implementing a restriction (e.g. an oil import fee) against third country products.

Article 904: Other Export Measures

904(a) clarifies the way in which proportionality and export price disciplines will apply in any situation in which either Party implements export controls for such GATT reasons as short supply, conservation, or domestic price stabilization schemes. The proportionality test for energy is identical to that provided in Article 409 for other goods.

904(b) acknowledges that higher prices for export sales might arise from the application of a quantitative restriction but, otherwise, should not be imposed by government action.

904(c) provides that if energy export restrictions are put in place for reasons relating to conservation, short supply or domestic price stabilization schemes, then governments may not require disruption of normal channels of supply or normal product mixes.

Article 908: International Obligations

This article refers to the International Energy Agency's Agreement on an International Energy Program (IEP) relative to oil, to which both Canada and the U.S. are already signatories; it makes clear that, in the event of any unavoidable inconsistency between the FTA and that 1974 Agreement, the provisions of the IEP will apply.

Annex 905.2: Regulatory and Other Measures

Paragraph 1 makes clear that it is the third National Energy Board (NEB) price test which is to be eliminated. This test compares the prices in export contracts to those for the least cost alternative for the export customer. The NEB can continue to operate its other price tests relative to the recovery of costs and the price available to Canadians for comparable service.

Paragraph 4 makes clear that, consistent with the Agreement, surplus tests can continue to be operated by either Party (e.g. by the NEB in Canada).

Chapter 10: Trade in Automotive Goods

There has been no substantive change from the Elements of Agreement. The provisions in the Elements of the Agreement on automotive tariffs, duty drawbacks, and foreign trade zones are not part of Chapter 10 since the general treatment provided for these subjects in Chapters 3 and 4 cover trade in automotive goods.

Article 1003: Import Restrictions

This article specifies the schedule for phasing out the embargo on used vehicles, such that after five years, there are no restrictions on the import of used automobiles and other motor vehicles.

Article 1005: Relationship to Other Chapters

This article contains a provision which would allow manufacturers to average their calculations for purposes of meeting the rule of origin.

Article 1006: Definitions

This article contains definitions of terms used in the automobile chapter.

Annex 1002.1

This three-part annex lists the companies eligible for various forms of waivers of customs duties.

Chapter 11: Emergency Action

Article 1101: Bilateral Actions

1101.2(d) provides that on termination of a bilateral safeguard action, the rate of duty shall be the rate which would have been in effect but for the emergency action.

1101.2 (b) and 1101.3 provide that actions may be taken after the transition period or may extend beyond the transition period only with the consent of the other Party.

Chapter 12: Exceptions for Trade In Goods

Article 1203 (c): Miscellaneous Exceptions (Fish)

The Elements of the Agreement provided for initiatives (elimination, phase-out, grandfathering) for an illustrative list of quantitative restrictions.

Article 1203 (c) elaborates on the list by grandfathering existing east coast provincial acts, some of which have been used to control the movement of unprocessed fish. They include the relevant provincial legislation in Quebec, Nova Scotia, New Brunswick, Prince Edward Island and Newfoundland. With respect to restrictions on British Columbian exports of unprocessed fish, the two governments are pursuing at this time their rights and obligations under GATT in light of the recent panel finding.

Article 1204: Beer and Malt Containing Beverages

Beer was not dealt with in the Elements of the Agreement in a separate fashion. In the Wine and Distilled Spirits chapter, it was specifically stated that it did not apply to beer.

The treatment of beer is now explicitly laid out in the text under chapter 12 exceptions. Article 1204 applying to beer and malt-containing beverages makes it explicit that national treatment as spelled out in Chapter 5 does not apply to existing measures for beer and malt-containing beverages (beer, coolers).

Article 1204 grandfathers all existing practices concerning beer. The effect of this article is that existing practices cannot be challenged under the FTA. For future practices, beer will have access to the full range of dispute settlement protection of the FTA. (The U.S. has not, however, relinquished its GATT rights with respect to existing practices respecting beer).

PART THREE: GOVERNMENT PROCUREMENT
Chapter 13: Government Procurement

Articles 1301 to 1309: Government Procurement

Chapter 13 on government procurement of goods specifies the federal government entities covered by the agreement, sets out the transparency provisions or procedures that will govern how procurements are conducted, and outlines a joint commitment to work towards further multilateral improvements in the GATT Government Procurement Code. It sets out in detail expanded procedural obligations for the purchases covered, including national treatment for all potential goods suppliers of both countries at all stages of the procurement process (pre-notification, tendering and bidding, evaluation of bids and awarding of contracts). A common rule of origin is defined for eligible goods.

Annex 1304.3: Entities Covered

The annex incorporates the GATT procurement Code and lists in all the federal departments and agencies covered for Canada and the U.S.

Annex 1305.3: Principles Guiding Bid Challenge Procedures

The annex outlines bid challenge principles, which will ensure that a reviewing authority shall accord timely and impartial consideration to any complaint or bid challenge by any supplier.

PART FOUR: SERVICES, INVESTMENT AND TEMPORARY ENTRY
Chapter 14: Services

The chapter establishes rules regarding the provision of commercially-traded services, listed in the coverage annex, across the border and within each country. These rules will apply for all future laws and regulations adopted by governments in regulating the service sectors covered by the Agreement.

Article 1401: Scope and Coverage

This article clarifies that the services chapter provides no additional rights or obligations regarding investment in the services industries. It states that establishment and acquisition of services industries are covered in the Investment chapter.

Article 1402: Rights and Obligations

1402.2 states that a province or state shall accord to persons of the other country treatment no less favourable than the most favourable treatment accorded to persons in the country of which it is a part.

1402.9 states that, with respect to trade in services, there are no obligations arising under this agreement regarding subsidies or government procurement practices.

Annex 1408: Services covered by the agreement

This annex lists a wide range of commercially-traded services covered by the agreement. Services provided by government and social services such as child care are excluded, as are cultural industries, legal services, all transportation modes and basic telecommunications. Financial services other than insurance are dealt with in a separate chapter.

Annex 1404.1.B: Tourism

Both parties have agreed not to use departure taxes or fees or currency restrictions to impede trade in tourism. Tourism-related services of a financial nature are included in the definition of tourism services.

Annex 1404.1.C: Computer Services and Telecommunications Network-Based Enhanced Services

The definition of basic and enhanced services will be as defined and classified by the respective regulators. No further benchmarks for these definitions have been included in the trade agreement.

The annex explicitly excludes any obligations regarding the establishment of facilities and offering of basic telecommunications transport services.

When a monopoly provider of basic telecommunications services competes in the provision of enhanced services, it may not engage in anticompetitive practices in the enhanced market. Separate accounting and other requirements shall ensure the separation of monopoly and competitive activities.

Annex: Transportation

The Elements of the Agreement stated that, subject to review by both parties, an annex would be included that clarifies the application of the agreement to future laws and regulations in the transportation section.

There is no transportation Annex because the U.S. was unable to bring the shipping industry under the discipline of the Services Code. No modes of transportation services are covered by the Services Code.

Chapter 15: Temporary Entry for Business Persons

Chapter 15 provides for temporary entry for a variety of business persons. Schedule 1 lists the general service providers who are covered. Schedule 2 lists the professions covered by the new provisions for professionals.

Chapter 16: Investment

The investment text has been clarified to make specific Canada's right to retain Canadian ownership of existing Crown corporations that are privatized and to preserve existing Investment Canada threshold levels and performance requirements for review of energy acquisitions.

Article 1601: Scope and Coverage

1601.2 provides for the exclusion of transportation and financial services (except insurance) and investments relating to government procurement.

Article 1602: National Treatment

1602.4 provides that for a province or state national treatment means treatment by a province or state to investors of a Party no less favourable than the most favourable treatment accorded investors of the country to which it belongs.

1602.5 provides that any existing business operated by a Canadian federal or provincial government is exempted from the national treatment provisions of 1602.1 and 1602.2. Consequently, measures can be imposed on the sale of these businesses such that they can be sold only to Canadians, and conditions can be imposed requiring control in the future by Canadians.

1602.6 provides that once a measure is introduced under 1602.5, it cannot be amended to make it more restrictive.

1602.7 provides that if subsequent to the entry into force of the agreement, a Canadian federal or provincial government acquires or creates a new business, this business is exempt from the national treatment provisions of 1602.1 and 1602.2 for the initial resale of the business to private investors. While these businesses can be sold only to Canadians, there would be no restriction beyond existing grandfathered legislation on the subsequent sale of the businesses.

Article 1603: Performance Requirements

1603 proscribes the imposition of significantly trade distorting performance requirements. It does not limit Canada's ability to negotiate local employment, product mandate, technology transfer, or research and development undertakings with investors. Moreover, there are no restrictions on the use of performance requirements related to subsidies or government procurement.

Article 1604: Monitoring

This provision permits requirements to be placed on an investor from the other country to provide information for monitoring purposes.

Article 1609: Taxation and Subsidies

This article provides that the provisions of the Investment Chapter shall not apply to any subsidy or any new taxation measures unless such subsidy or taxation measures unjustifiably discriminate between investors of the Parties or constitute a disguised restriction on the benefits accorded to investors under the Investment Chapter.

1602.8 allows for different treatment of investors from the other Party to the extent required for prudential, fiduciary, health and safety or consumer protection reasons, and the where different treatment is equivalent in effect to the treatment accorded to the investors of the Party for such reasons.

Annex 1607.3

Paragraph 4, stipulates that in amending the Investment Canada Act, the oil, gas, and uranium industries will be exempted from the changes. This means that threshold levels for investment review will not be raised and the FTA's performance requirement restrictions will not apply to these industries.

PART FIVE: FINANCIAL SERVICES

Chapter 17: Financial Services

Articles 1701: Scope and Coverage

Article 1701 sets out the relationship of this Chapter to the rest of the FTA. Among other things, it specifies which Articles of the Agreement apply. Accordingly, the dispute settlement process, the investment chapter (other than insurance services) and the services code do not apply. It also specifies that the commitments of this chapter do not apply to provincial or state laws governing financial institutions.

PART SIX: INSTITUTIONAL PROVISIONS

Chapter 18: Institutional Provisions

Chapter 19: Binational Panel Dispute Settlement in Antidumping and Countervailing Cases

Article 1904: Final Antidumping and Countervailing Duty Determinations

The Elements of the Agreement refer to "final orders" arising from determinations issued by the Department of Commerce and the International Trade Commission. The text defines "final orders" as including both positive and negative final determinations.

To maintain the integrity of the panel process, 1904.13 creates an "extraordinary challenge procedure" to allow a Party to challenge a decision where a member of the panel may be biased or where the panel has departed from a fundamental rule of procedure, or has manifestly exceeded its powers. This procedure is an extraordinary one and is not intended to allow for a review of the merits of the panel decision. By establishing such a procedure, there will be no need for domestic review where there are allegations of bias or excess of jurisdiction.

1904.5 provides for maintaining the rights of individuals to judicial review in anti-dumping and countervailing duty cases. Canada, upon the request of an individual, will request the establishment of a Panel if that individual would otherwise have had such rights under the domestic laws of Canada. The situation will be similar in the United States.

Article 1911: Definitions: Final Determinations

To permit importers and exporters of both Canada and the United States a balanced opportunity in antidumping and countervailing duty cases, the Special Import Measures Act and the Federal Court Act will be amended to permit review by the panel of certain final determinations of the Deputy Minister of National Revenue. This ensures that these final determinations will be subject to review in both countries.

Annex 1901.2: Membership of Panels

A majority of the five-member panel including the chairman will be lawyers, given that the panel replaces judicial review. However, in light of the breadth of the Trade Agreement, non-lawyers with familiarity with international trade law are also eligible to serve as panelists.

Chapter 20: Other Provisions

Article 2001: Tax Convention

This provision affirms that the existing tax convention between Canada and the United States continues to be fully operational. Nothing in the Free Trade Agreement affects the rights and obligations resulting from the tax convention.

Article 2002: Balance of Payments

2002 acknowledges each country's rights, now existing under international agreements, to take necessary restrictive actions for balance of payments reasons.

Article 2006: Retransmission Rights

2006 clarifies the understanding that each Party may determine the condition under which the right to equitable remuneration for any retransmission will be exercised. It also provides by 1990 for the establishment of a joint committee to review retransmission issues in both countries.

Article 2007: Advertising in Canadian Periodicals and "Print in Canada"

The final text amplifies upon Canada's agreement to remove the "print and typeset in Canada" requirement in Section 19 of the Income Tax Act. This will enable Canadian publishers to source their printing requirements for Canadian magazines and periodicals with the most efficient and effective printers in Canada or the U.S. and thereby ensure a competitive manufacturing environment for Canadian publishers.

Article 2010: Monopolies

The article provides that either Party may maintain or designate a monopoly. There are obligations to contain the impact of a monopoly on: discrimination in the provision of monopoly goods or services, and anticompetitive practices by the monopolist in any other market.

These provisions protect Canada's current federally and provincially regulated monopolies, and our rights to maintain and create new monopolies. The obligations to provide monopoly services on a non-discriminatory basis, and to prevent the monopolist from using its power to undertake anticompetitive practices in other markets are standard and well-established practices in Canada that will not affect the operation of current or future initiatives.

Postal Rates for Magazines

Canada has no obligation to phase out discriminatory postal rates for magazines of significant circulation. The U.S. tried to go beyond the October 4 Elements of the Agreement to phase out the difference (1.5 cents) between Code 3 and Code 6 periodicals and Canada refused.

Chapter 21: Final Provisions**Article 2106: Duration and Termination**

This article specifies that the agreement shall remain in force unless terminated on six month's notice. Six month's termination is a requirement of the U.S. Trade Act for agreements negotiated under fast track authority.